HUANG EE HOE & ANOR.

v.

TIONG THAI KING & ORS.

HIGH COURT BORNEO, SIBU
CHONG SIEW FAI J
[SUIT NO. 54 OF 1984]
4 OCTOBER 1990

COMPANY LAW: *Preliminary issues - Whether prima facie case established - Locus standi of plaintiffs to commence action on behalf of company - Derivative action.*

CIVIL PROCEDURE: *Disposal of preliminary issue prior to actual trial - Saving time and money.*

The defendant/applicants D1, D2 , D3 and D4 asked for the determination of certain issues namely

(a) whether the plaintiffs have established a *prima facie* case as alleged against the company (SBS) D5 and

(b) whether the company should be the one to bring an action against an alleged wrong done to the company.

These issues were raised based on the *Prudential Assurance Co.* case.

The plaintiffs replied that they were legally entitled to sue the defendants on a derivative basis of the shareholders "B" of SBS (see preceding case) and objected to D1, D2, D3 and D4's application.

Counsel for the plaintiffs argued that in this case, as complex issues were involved, there was a necessity for a full trial; further that issue *estoppe*l applied.

Held:

[1] It is necessary to bear in mind that what was stated to be required in *Prudential Assurance* case respecting the two issues in question is that a prima facie case be made out. The reasoning for such a course is, as explained in *Prudential Assurance* case, *supra,* to avoid unjustifiably subjecting the company to a full trial in order to enable the Court to determine whether the plaintiffs were entitled in law to make the company undergoing the entire action.

[2] It appears that the inference to be drawn from *Prudential Assurance* case is that a derivative action is unlikely to be allowed to go on unless the plaintiffs show a prima facie case of entitlement to the relief claimed and of control of the company by the alleged wrongdoers, who are using their controlling power to prevent the action from being brought by the company.

[3] Where there are independent directors or shareholders, it is implicit from the judgment in *Prudential Assurance* case that their views are weighty and important. Where, as it appears in our instant case, an independent component is lacking, the Court nevertheless has to deal with the preliminary issues, if raised, by considering the stand-points of the directors or shareholders of both sides.

[4] The application should, be allowed to proceed subject, however, to certain modifications.

[5] Leaving the issues for disposal at the commencement of trial of the main action necessarily means that all are set for the trial including the subpoena and presence or attendances of witnesses of both sides in participation of the trial to proceed. On the other hand, if the preliminary issues are disposed of in advance, preparatory works for the trial as aforesaid may or may not be necessary dependent upon the result of the present application. An early disposal of the present application would undoubtedly place parties in a clearer position as to whether anything needs to be done in the conduct of the case, and is to be preferred.

[Order accordingly.]

Cases referred to:
Prudential Assurance Co. Ltd. v. Newman Industries Ltd. & Ors. (No. 2) [1982] 1 All ER 354
Foss v. Harbottle [1843] 2 Hare 461
Burland v. Earle [1902] AC 83
Paidiah Genganaidu v. Lower Perak Syndicate Sdn. Bhd. & Ors. [1974] 1 MLJ 220
Smith v. Croft (No. 2) [1987] 3 All ER 909
Tilling v. Whiteman [1979] 1 All ER 737
Chan Kum Loong v. Hii Sui Eng [1980] 1 MLJ 313
Carl-Zeiss-Stiftung v. Herbert Smith [1968] 2 All ER 1002

For the Plaintiffs/Respondents - George Lo; M/s. Nashir, Johal & Co.
For the Defendants/Applicants - H.C. Sim; M/s. Reddi & Co.

JUDGMENT

Chong Siew Fai J:

Ruling on 1st, 2nd, 3rd and 4th Defendants' summons dated 1 March 1990

By a summons dated 1 March 1990 the applicants that is the 1st, 2nd, 3rd and 4th defendants (collectively called the defendants) seek for an order that:

(i) the following questions or issues raised in para. 2(ii) of the defence and para. 1 of the reply to defence be tried and determined as preliminary questions or issues before all other questions and issues in this action, namely:

(a) whether the plaintiffs have established a *prima facie* case that Sarawak Building Supplies Sdn. Bhd. (the company) is entitled to the reliefs claimed in the amended writ of summons and the amended statement of claim filed herein?

(b) whether the plaintiffs are barred from bringing this action by the rule that the proper plaintiffs in an action in respect of an alleged wrong done to the company is the company itself and not its shareholders? and

(c) whether the plaintiffs fall within any exceptions to that rule on the basis of the matters disclosed in the amended statement of claim?

(ii) that such directions as this Honourable Court may deem fit, be given for the trial or determination of the said preliminary questions or issues; and

(iii) that the costs of and occasioned by this application be costs in the action.

Since the issue of the summons, the defence has been amended. However, para. 2(ii) of the defence mentioned in item (i) of the relief sought remains unchanged. Paragraph 2(ii) reads:

> The 1st, 2nd, 3rd and 4th defendants (hereinafter collectively referred to as "the defendants") deny that the plaintiffs were and are legally entitled to maintain this action or at all.

Paragraph 1 of the plaintiffs' reply pleads:

> As regards para. 2(ii) of the defence, the 1st and the 2nd plaintiffs will say that they are legally entitled to sue the defendants, including the 5th defendant, in the nature of a derivative action for and on behalf of themselves and for and on behalf of the other "B" shareholders of the 5th defendant-company. The ruling of the honourable Court dated 15 December 1988 is pertinent.

Relying on *Prudential Assurance Co. Ltd. v. Newman Industries Ltd. & Ors. (No. 2)* [1982] 1 All ER 354, the defendants through Mr. Fong wished the issues framed to be determined.

For the plaintiffs, Mr. Lo objected to the application on grounds which I shall with deal in a moment.

The basic rule of the law is that the only proper plaintiff in proceedings to redress a wrong against a company or to enforce a right of a company is the company itself. (*Foss v. Harbottle* [1843] 2 Hare 461; *Burland v. Earle* [1902] AC 83 at 93; *Paidiah Genganaidu v. Lower Perak Syndicate Sdn. Bhd. & Ors.* [1974] 1 MLJ 220 FC. This rule has come to be known as the rule in *Foss v. Harbottle*. However, difficulties and injustice arose where the majority of the directors or shareholders were the wrongdoers or benefited by the wrong because they would not sanction the bringing of actions by the company. To overcome the problem, exceptions to the rule have developed where minorities can bring a 'derivative action' (a term originated in the United States) on behalf of themselves and all the other shareholders (except the wrongdoer) against the wrongdoers, joining also the company as a defendant. One of such exceptions is where there is allegedly fraud on the minority and the wrongdoers are in control of the company. (*Burland v. Earle* [1902] AC 83 at 93).

Prudential Assurance Co. Ltd. v. Newman Industries Ltd. (No. 2) [1982] 1 All ER 354 CA relied on by the plaintiffs was a derivative action. It appears clear from that case that before such an action is allowed to proceed, the defendants are entitled to ask for determination as a preliminary issue whether the plaintiffs have established a prima facie case:

(i) that the action falls within the proper boundaries of the exception to the rule in *Foss v. Harbottle*; and

(ii) that the company is entitled to the relief claimed.

The relevant part of the judgment on the point and the reasoning therefor are reproduced below: [at 365-366]

> We desire however to say two things. First, as we have already said, we have no doubt whatever that the Judge erred in dismissing the summons of 10 May 1979. He ought to have determined as a preliminary issue whether the plaintiffs were entitled to sue on behalf of Newman by bringing a derivative action. It cannot have been right to have subjected the company to a 30-day action (as it was then estimated to be) in order to enable him to decide whether the plaintiffs were entitled in law to subject the company to a 30-day action. Such an approach defeats the whole purpose of the rule in *Foss v. Harbottle* and sanctions the very mischief that the rule is designed to prevent. By the time a derivative action is concluded, the rule in *Foss v. Harbottle* can have little, if any, role to play. Either the wrong is proved, thereby establishing conclusively the rights of the company, or the wrong is not proved, so cadit quaestio.
>
> The second observation which we wish to make is merely a comment on the Judge's decision that there is an exception to the rule in *Foss v. Harbottle* whenever the justice of the case so requires. We are not convinced that this is a practical test, particularly if it involves a full-dress trial before the test is applied. On the other hand we do not think that the right to

> bring a derivative action should be decided as a preliminary issue on the hypothesis that all the allegations in the statement of claim of 'fraud' and 'control' are facts, as they would be on the trial of a preliminary point of law. In our view, whatever may be the properly defined boundaries of the exception to the rule, the plaintiff ought at least to be required before proceeding with his action to establish a prima facie case (i) that the company is entitled to the relief claimed and (ii) that the action falls within the proper boundaries of the exception to the rule in *Foss v. Harbottle*.

It should perhaps be noted that the observation on procedure in the judgment quoted above is clearly obiter because when the Court of Appeal (English) made the pronouncement, the whole action had been heard and determined and, also, the company, Newman Industries Ltd. had intended to accept the decision on the case made in its favour with the result that the question of whether the plaintiff was entitled to bring the derivative action was no longer relevant. On the other hand, the procedure was adopted and similar issues considered in subsequent derivative actions. See *e.g. Smith v. Croft (No. 2)* [1987] 3 All ER 909.

Though conceding *Prudential Assurance Co. Ltd. v. Newman Industries Ltd. (No. 2)* [1982] 1 All ER 354 a persuasive authority, Counsel for the plaintiffs/respondents, in the attempt for the plaintiffs/respondents, in the attempt to dissuade me from following it, submitted that the facts and the law in our instant case were closely and inseparably interwined, that complex issues were involved, and that considerable details of fact including question of fraud needed to be gone into which could only be done in a full trial. For the applicants, Mr. Fong stated that the issues under the summons involved examination of pleadings on which he would solely rely and that little evidence would be required. As regards the voluminous documents reflected in List of Documents filed under the discovery, he pointed out that they largely consisted of invoices and log lists.

It is necessary to bear in mind that what was stated to be required in *Prudential Assurance Co. Ltd. v. Newman Industries Ltd. (No. 2)* [1982] 1 All ER 354 respecting the two issues in question is that a prima facie case be made out. The reasoning for such a course is, as explained in *Prudential Assurance* case, *supra*, to avoid unjustifiably subjecting the company to a full trial in order to enable the Court to determine whether the plaintiffs were entitled in law to make the company undergoing the entire action.

The observations about trials of preliminary issues of law and fact expressed in *Tilling v. Whiteman* [1979] 1 All ER 737 and *Chan Kum Loong v. Hii Sui Eng* [1980] 1 MLJ 313 are, in my opinion, inapplicable in our instant case. The 2 cases are not derivative actions. The question of exception to the rule of *Foss v. Harbottle* does not arise. It appears to me that the inference to be drawn from *Prudential Assurance Co. Ltd. v. Newman Industries Ltd. (No. 2)* [1982] 1 All ER 354 is that a derivative action is unlikely to be allowed to go on unless the plaintiffs show a prima facie case of entitlement to the relief claimed and of control of the company by the alleged wrongdoers, who are using their controlling power to prevent the action from being brought by the company. Trial of the preliminary issues is to this end.

Next, it was contended for the plaintiffs/respondents that *Prudential Assurance Co. Ltd. v. Newman Industries Ltd. (No. 2)* [1982] 1 All ER 354 was distinguishable, that, unlike *Prudential Assurance* case, there was no independent board in our case, that the 5th defendant-company, Sarawak Building Supplies Sdn. Bhd., did not engage any Counsel and had not assumed the position that the advantageous outcome of the suit would be "vastly outweighed by harm inflicted upon it by the action...", and that, consequently, this Court need not and should not consider the question: "Ought I to be trying a derivative action?"

I find no merits in the contentions. Where there are independent directors or shareholders, it is implicit from the judgment in *Prudential Assurance Co. Ltd. v. Newman Industries Ltd. (No. 2)* [1982] 1 All ER 354 that their views are weighty and important. Where, as it appears in our instant case, an independent component is lacking, the Court nevertheless has to deal with the preliminary issues, if raised, by considering the stand-points of the directors or shareholders of both sides.

Mr. Lo, I noted, pointed to outcome of a shareholders' meeting held on the direction of the Court. That would be a matter for consideration in the hearing of the substantive application.

For the plaintiffs/respondents it was further argued that issue *estoppel* applied to the two preliminary issues raised in that they had been dealt with at the hearing of previous applications. I have gone through the matters raised in the previous proceedings. In this respect, I agree with Mr. Fong of Counsel for the applicants and I have no doubt that the issues contained in the present summons had not been decided. A clear indication of that may be seen in my ruling on 15 December 1988, particularly pp. 3-4 thereof.

The application should, in my view, be allowed to proceed subject, however, to the modifications stated below. The modifications are in keeping with the *obiter dictum* in *Prudential Assurance Co. Ltd. v. Newman Industries Ltd. (No. 2)* [1982] 1 All ER 354 at 366 upon which the applicants heavily, and, I would say, solely rely for this application. Furthermore, the issues suggested in *Prudential Assurance* case are not pure questions of law. Facts are necessarily involved. Having regard to O. 33 r. 2 relied on by the defendants/ applicants which also empowers the Court to direct the manner in which a question is to be stated and adhering as best as possibly could to the applicants' original framing of the issues bearing in mind, at the same time, the guidance in *Prudential Assurance Co. Ltd. v. Newman Industries Ltd. (No. 2)* [1982] 1 All ER 354, I would order the following modifications to the issues appearing in the summons:

(i) delete the last word "and" appearing in prayer (i)(b) of the summons, and substitute therefore the word "or", and

(ii) delete the words "on the basis of the matters disclosed in the amended statement of claim?" and substitute therefore the words: "which permits minority shareholders to bring an action, in other words, within any exceptions to the rule in *Foss v. Harbottle*".

After modification, prayers (i)(b) and (c) read thus:

(b) whether the plaintiffs are barred from bringing this action by the rule that the proper plaintiffs in an action in respect of an alleged wrong done to the company is the company itself and not its shareholders? or

(c) whether the plaintiffs fall within any exceptions to that rule which permits minority shareholders to bring an action, in other words, within any exceptions to rule in *Foss v. Harbottle.*

The applicants, in my view, are not in any way prejudiced by the alteration to prayer (i)(c) for it seems to me that any attempt sought to have the action dismissed or struck out by reason of any alleged defective pleading may be made under the applicants' summons dated 3 July 1984 which, as the proceedings in this action indicate, the applicants have every intention to pursue.

Finally, for the plaintiffs/respondents, it was urged upon me that if the application were to be allowed, the preliminary issues be dealt with at the commencement of the trial of this action. I am unable to accept this. Leaving the issues for disposal at the commencement of

trial of the main action necessarily means that all are set for the trial including the subpoena and presence or attendances of witnesses of both sides in participation of the trial to proceed. On the other hand, if the preliminary issues are disposed of in advance, preparatory works for the trial as aforesaid may or may not be necessary dependent upon the result of the present application. An early disposal of the present application would undoubtedly place parties in a clearer position as to whether anything needs to be done in the conduct of the case, and is, in my opinion, to be preferred.

As stated by Lord Denning MR in *Carl-Zeiss-Stiftung v. Herbert Smith* [1968] 2 All ER 1002 at 1004:

> The true rule was stated by Romer LJ in *Everett v. Ribbands* (3):
>
> Where there is a point of law which, if decided in one way, is going to be decisive of the litigation, advantage ought to be taken of the facilities afforded by the rules of Court to have it disposed of at the close of pleadings or very shortly afterwards.
>
> I have always understood such to be the practice.

Romer LJ, of course, was referring to issue of point of law. The observation on timing, in my opinion, equally applies to the issues raised and modified in the present summons.

Except for the normal adjournment on 14 May 1990, costs hitherto incurred in the hearing of this summons be reserved.

Quite detached from present application, Mr. Lo, in the course of his submission, had asked for early hearing of the applicants' summons dated 10 May 1990 applying for an earlier trial of this action. I suggest that the request be made to the Senior Assistant Registrar. However, in view of the nature of the relief sought in the application presently under consideration, there ought, I trust, be no objection that the said summons be heard after the disposal of the issues earlier on stated herein.

Also found at [1991] 1 CLJ 381